



**COUNTY OF LOS ANGELES
DEPARTMENT OF AUDITOR-CONTROLLER**

KENNETH HAHN HALL OF ADMINISTRATION
500 WEST TEMPLE STREET, ROOM 525
LOS ANGELES, CALIFORNIA 90012-2766
PHONE: (213) 974-8301 FAX: (213) 626-5427

J. TYLER McCAULEY
AUDITOR-CONTROLLER

December 14, 2006

TO: Each Board Member
All Department Heads

FROM: J. Tyler McCauley
Auditor-Controller

SUBJECT: **ADJUSTMENTS AFFECTING YEAR-END AND NEW YEAR PAY CHECKS**

At the end of each year, net pay for many of you will begin to fluctuate as limits for deferred earnings are reached. In addition, we must process adjustments for various programs unique to Board members and department heads that may affect your taxable income and W-2 Wage and Tax Statements. Some of these adjustments appear on your pay stubs and some affect your net pay; all are reflected on your W-2s.

In addition, fluctuations in net pay may occur for some of you as we cross over between two tax years and deferred earnings deductions resume. All of you will see changes in net pay as the new federal and State withholding changes are implemented in the new calendar year. This letter provides you with information that will assist you in understanding and planning for these payroll processes.

Supplemental Life Insurance Program (commonly referred to as the Split Dollar Life Insurance Program)

Pursuant to County Code Section 5.39.030 – "Supplemental Life Insurance", the County of Los Angeles pays the monthly premium for department heads and County officers. Since this life insurance coverage is provided at no cost to you, it must be treated as a taxable fringe benefit. The amount that is taxable is considered "imputed income", based on IRS tables, and determined by the insurance broker, William Mercer, Inc.

We received these amounts from the Department of Human Resources and processed them through the payroll system for the December 15, 2006 payday. The amount was added to your normal taxable wages, and all applicable federal, State, and HIT taxes were withheld. Because this amount is included in the deduction base for calculating tax deferred deductions, deduction amounts withheld for the Savings Plan and for the

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Horizons Plan increased if you have not yet reached the annual maximums and you may see a decrease in your net pay on this payday. The imputed income amount was reflected in the "Imputed Income" box on your December 15, 2006 pay stub, and added to any Megaflex/Flex Plan life insurance imputed income and/or SIB life insurance imputed income amounts that you normally see each month. Finally, this imputed income amount will be reported as taxable wages on your W-2 Wage and Tax Statement for 2006.

Transportation Allowance

Pursuant to County Code Section 5.40.465 titled "Transportation Allowance", any department head or County officer may elect to receive a transportation allowance in lieu of an assigned or leased County vehicle. If you have elected to receive the Transportation Allowance, you will see the amount as earnings code 050 (TRANS ALLOW) on your pay stub each month. This amount is included as taxable income and taxed each month, just like your regular earnings, and will be included in the Wages, Tips, and Other Compensation box on your W-2 for 2006.

Assigned Vehicle

If you have elected not to receive the transportation allowance and have been assigned a County vehicle for all or part of the year, the value of the personal use of the vehicle is a taxable fringe benefit (Imputed Income) per the IRS. In most cases, the personal use of an assigned vehicle will be valued at \$3.00 per day, and it must be reported as taxable income on the W-2.

If you have an assigned County vehicle, we processed a payroll transaction to include the value of this benefit on the December 15, 2006 payday. Like the Split Dollar Life Insurance processing, this amount was not paid but is added to your normal taxable wages, and all applicable federal, State, and HIT taxes were withheld, and this amount is included in the deduction base for calculating tax deferred deductions. The amount was reflected in the "Imputed Income" box on your December 15, 2006 pay stub, and added to any Megaflex/Flex Plan life insurance imputed income and/or SIB life insurance imputed income amounts that you normally see each month. This additional imputed income may have caused a decrease in your net pay on this payday. This amount will be included in the Wages, Tips, and Other Compensation box on your W-2 for 2006, and will be reported as itemized information in Box 14 (Fringe Benefits).

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Deferred Income Plans

The following are the IRS limits on taxable earnings that can be deferred under the various plans for 2006:

- If you are participating in the Savings Plan only (deduction code 138 on your pay stub), you may defer \$15,000 (\$20,000 if you are 50 or over).
- If you are participating in the Horizons Plan only (deduction code 137 on your pay stub), you may defer \$15,000 (\$20,000 if you are 50 or over).
- If you are participating in the accelerated Horizons Plan only (deduction code 136 on your pay stub), you may defer \$30,000 (twice the regular Horizons limit).
- If you are participating in both the Savings and Horizons Plans and elected the 'aggregate limit', you may defer \$8,500 combined. If you elected the higher 'individual limits', you may defer \$15,000 (\$20,000 if you are 50 or over) in the Savings Plan, and \$15,000 (\$20,000 if you are age 50 or over) in the Horizons Plan.
- If you are participating in both the Savings Plan (code 138) and accelerated Horizons Plan (code 136) you may defer \$15,000 (\$20,000 if over 50 years of age) in the Savings Plan, and \$30,000 in the accelerated Horizons Plan.

If you reached your limits for 2006 prior to the December 15, 2006 payday, your deductions have already stopped. If you have already reached your limit, or reached your limit on the December 15, 2006 payday, and you remain an active participant for 2006, the entire amount of your deferred deduction(s) from December 2006 earnings will be taken from the January 12, 2007 pay check and you can expect a reduction in net pay on this payday. In other words, on the January 12, 2007 payday, you will have a full month's deduction withheld rather than the normal half a month's deduction. As we cross over between two tax years, and if you have reached the limit(s), continuing deductions for deferred earnings from December are treated differently from other months in the year when we normally split the monthly deduction amount in half each payday. Beginning with the January 30, 2007 payday, the deferred earnings deductions will again be split.

If you did not reach the deferred limit(s) in 2006, the deductions for your deferred plans will continue to be split between your December 29, 2006 and January 12, 2007 pay checks as usual.

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Megaflex/Flex Plan

Monthly premiums for most medical and dental plans increased for Plan Year 2007. The new rates for Megaflex/Flex Plan benefits will be reflected on your January 12, 2007 pay check based on the benefit selections you made through the open enrollment process. You may have made a change to your Health Care or Dependent Care spending account(s) deduction amount(s), changed a medical or dental plan provider, or added or removed a dependent from medical or dental insurance coverage. These and other changes will result in more or less taxable cash (036 – FLEX EARN), a pre-tax cafeteria deduction (140 – SALARY RED) greater or less than the prior year, or a transition from taxable cash to payroll deduction or vice versa.

For Plan Year 2007, your Group Term Life Insurance coverage will be replaced with Group Variable Universal Life (GVUL) Insurance coverage. IRS regulations require premiums for Group Variable Universal Life Insurance coverage be paid as an after tax deduction outside of the cafeteria plan. If you elected Universal Life Insurance coverage, you will see a deduction under a deduction code between 800 and 844 on your January 12, 2007 pay stub. The actual deduction code that you will see on your pay stub will depend on the coverage that you elected. If you elected to participate in the GVUL Investment feature, you will see deduction code 845 on your pay stub.

Federal and State Income Tax

Changes to the federal and State income tax withholding tables will be in place effective January 1, 2007 for all wages paid on and after this date. These rates will first be reflected in your January 12, 2007 pay check. Taxes will be calculated and withheld based on the filing status we have on file for you in accordance with these charts.

If you have any questions on any of the above matters, please call me. Some of your staff will also be affected by Assigned Vehicles, Deferred Income Plan limits, Megaflex/Flex Plan selections and withholding changes. Your payroll staff should be able to answer their questions.

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RD:GI:JY